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UGI CORPORATION

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December 1, 2009

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PA PUBLIC UTILITY COMMISSION
SECRETARY'S BUREAU

James J. McNulty, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street
Harrisburg, PA 17120

Re: Proposed Rulemaking: Natural Gas Distribution Company Business Practices; 52 Pa. Code §§ 62.181-62.185, Docket No. L-2009-2069117

***SEARCH Final Order and Action Plan* for Increasing Effective Competition in Pennsylvania's Retail Natural Gas Supply Services Market, Docket No. I-00040103F0002**

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PA PUBLIC UTILITY COMMISSION
SECRETARY'S BUREAU

Dear Secretary McNulty:

Enclosed for filing, please find an original and fifteen copies of the comments of the UGI Distribution Companies. Should you have any questions concerning this filing, please feel free to contact me.

Very truly yours,

Mark C. Morrow

Counsel for the UGI Distribution Companies

460 NORTH GULPH ROAD, KING OF PRUSSIA, PA 19406

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BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Proposed Rulemaking: Natural Gas Distribution Company Business Practices; 52 Pa. Code §§ 62.181-62.185	:	Docket No. L-2009-2069117
SEARCH Final Order and Action Plan for Increasing Effective Competition in Pennsylvania's Retail Natural Gas Supply Services Market	:	Docket No. I-00040103F0002

COMMENTS OF THE UGI DISTRIBUTION COMPANIES

UGI Central Penn Gas, Inc. ("CPG"), UGI Penn Natural Gas, Inc.("PNG"), and UGI Utilities, Inc. – Gas Division ("UGI") (collectively the "UGI Distribution Companies") appreciate this opportunity to submit comments in response to the Commission's May 1, 2009 Proposed Rulemaking Order in the above-captioned matter published in the October 17, 2009 edition of the *Pennsylvania Bulletin*. These comments are meant to supplement the comments filed by the Energy Association of Pennsylvania at this docket.

I. Cost Recovery

The UGI Distribution Companies commends the Commission for addressing cost recovery associated with the promotion of retail competition, but believe that the provisions of 52 Pa.Code §62.184 unnecessarily complicate the cost recovery process, and inappropriately requires the establishment of what will be a base rate surcharge in a

Section 1307(f) purchase gas cost proceeding subject to an abbreviated statutory procedural schedule.

A. Line Item Rate Making Concerns

The proposed regulations, amongst other things, would require NGDCs to (1) file a fully allocated cost of service study in a Section 1307(f) purchased gas cost proceeding, (2) identify costs associated with promoting competition currently reflected in existing base rates, (3) remove such costs from base rates by means of a credit and (4) recover these costs and presumably incremental costs resulting from SEARCH-related mandates through a reconcilable nonbypassable base rate surcharge "recovered on a per unit basis on each unit of commodity which is sold or transported over its distribution system without regard to the customer class of the end user." 52 Pa.Code §62.184.

The judicial doctrine prohibiting line item ratemaking recognizes that under traditional cost-of-service ratemaking procedures utilities have an important incentive to manage their costs between base rate cases by not having the option of recovering incremental increases of line item expenses outside of a general base rate case where costs and revenues can be considered holistically. Even under this doctrine, however, the Commission has authorized, amongst other things, the recovery of reasonably incurred government-mandated incremental costs between base rate cases without removing incentives to operate efficiently. Examples of such Commission-permitted incremental recovery include (1) the State Tax Adjustment Surcharge mechanism, (2) surcharges to recover the non-gas cost components of pipeline take-or-pay charges incurred under FERC mandates designed to open interstate pipelines to third party transportation, (3) universal service surcharges, (4) gas customer choice education expense surcharges and

(5) current electric customer education surcharges. In Popowski v. Pa.PUC, 869 A.2d 1144 (2005), *appeal denied* 895 A.2d 552, the Commonwealth Court held that Section 1307(a) surcharges cannot be used to recover return on capital investments, but went on to state:

> As we have previously held, a Section 1307(a) automatic rate adjustment is appropriate where expressly authorized, as in 66 Pa. C.S. § 1307(g), or for easily identifiable expenses that are beyond a utility's control, such as tax rate changes or changes in the costs of fuel.

Id. at 1160.

Here, the Commission anticipates requiring NGDCs to incur certain incremental expenses associated with promoting retail choice that will produce neither additional revenue nor reduced expenses. UGI believes the Commission could permit the recovery of these incremental expenses without running afoul of the prohibition against line item ratemaking and should do so. The Commission should also clarify that "incremental costs" means costs that but for the directed retail choice promotion requirements would not have been incurred by the NGDC. This should remove uncertainty, encountered by UGI in other contexts, over whether incremental costs are as described above or instead are only entirely new categories of costs. For example, expenses associated with modifying information systems to accommodate new retail choice mandates should be recoverable even if information system costs for existing retail choice systems were a category of costs addressed in a prior base rate proceeding.

B. Cost-of-Service Studies

Permitting cost recovery of incremental expenses would also presumably eliminate the incurrence of unnecessary expenses for preparing cost of service studies, which the proposed regulations would presumably require to identify the costs associated

with promoting competition in prior base rate filings. By simply permitting the recovery of incremental costs under the recognized exception to line-item ratemaking restrictions, however, the significant expenses of preparing such studies will be avoided. Moreover, even if such studies were produced, they would not necessarily identify the specific expenses of concern to the Commission. For example, a cost of service study may not be sufficiently specific or if, the prior base rate case was resolved through a black-box settlement it may not be possible to identify the expense recovery actually authorized. It should also be recognized that cost of service studies are highly complex and involve many discretionary decisions regarding how to allocate particular costs. The cost of service study is one of the most hotly contested issues in any base rate case. Parties often present multiple cost of service studies during rate cases using very different methodologies which reach very different cost allocation conclusions. To the extent the Commission seeks to have cost of service studies produced to address the recovery of costs by rate class, NGDCs could presumably track incremental cost incurrence by rate class without the preparation of expensive cost of service studies.

C. Proceedings where Surcharges would be Established

The proposed regulations would require surcharges for the recovery of retail competition promotion activities to be proposed and resolved in the context of annual Section 1307(f) purchased gas cost ("PGC") proceedings, and would further require annual adjustments to the surcharges to be performed at the same time as annual PGC adjustments.

While synchronizing adjustments to the proposed retail choice promotion surcharge with annual PGC adjustments may be appropriate, such synchronization can be achieved

even if the surcharge is established in a non-PGC proceeding. Moreover, it would be preferable for the surcharge to be established in a separate rate proceeding since annual PGC filings must operate on an abbreviated statutorily-mandated procedural schedule ill-suited for the establishment of a base rate surcharge, particularly if cost-of-service study requirements are required. Since the proposed surcharge would apply to non-PGC customers, establishing a retail choice promotion surcharge in a PGC proceeding could very well require the intervention of parties otherwise not subject to PGC rates, thereby further complicating annual PGC proceedings.

D. Nonbypassable Surcharge

Although the proposed regulations state the recovery of retail choice promotion costs should be through a "nonbypassable" surcharge, §68.184(c) states the "surcharge shall be recovered on a per unit basis on each unit of commodity which is sold or transported over its distribution system without regard to the customer class of the end user."

Some NGDCs have rates that are flexed down to prevent users from bypassing the distribution system or using alternate fuels, and surcharges on such rates are ineffective since additional revenues cannot be collected from such customers. UGI would suggest the relevant portion of §68.184(c) be modified to state: "surcharge shall be recovered in a competitively neutral manner on a per unit basis on each unit of commodity which is sold or transported over its distribution system without regard to the customer class of the end user except where competitive conditions prevent the collection of incremental revenues."

E. Removal of Existing Costs

It is unclear why the Commission has proposed the removal of existing retail choice promotion costs from base rates and for recovery through a reconcilable mechanism, rather than simply permitting the recovery of incremental costs. If the Commission believes there is a reason for this rate methodology, however, it should further explain what its objectives are. Moreover, if the proposed methodology is to be adopted, the Commission should, to avoid unnecessary litigation, determine if its intent is to permit the recovery of existing costs as they existed at the time of the last base rate case, or if it intends to permit the recovery of costs at their current level. For some companies the last base rate case predated the Customer Choice legislation, so it is unlikely certain of these costs would be included in rates.

II. Standard Business Practices

The Proposed Rulemaking Order indicates the Commission will establish a working to review strawman business standards, and will be looking to the recommendations of a subgroup of the SEARCH process that reviewed certain "NAESB wholesale gas nomination standards and retail business practices."

The UGI Distribution Companies applaud the Commission's decision to seek further input on this important issue and would note the following concerns as the Commission works to develop its strawman proposal.

First, the Commission should be aware that the SEARCH subgroup that reviewed the NAESB standards did not have a broad representation of NGDCs, and there was not a sufficient opportunity to comment on its recommendations. However, nonpartcipants did point out that the group was perhaps inappropriately reviewing NAESB wholesale

quadrant standards. Those standards, which govern interactions of interstate pipelines and storage operators with shippers under FERC rules may have little applicability to interactions of NGDCs with end use transportation customers or choice suppliers. For example, interstate pipelines are subject to certain capacity release standards that have no applicability to NGDC operations. Accordingly, to the extent the Commission looks to NAESB for developing its strawman proposal, it should look to NAESB retail quadrant standards for guidance.

Second, the Commission should be mindful of the distinctions between larger customer transportation service and services rendered to choice suppliers serving aggregated pool of smaller essential human needs customers. Even before the passage of the Natural Gas Choice and Competition Act ("Choice Act"), larger volume customers received transportation service and procured their own upstream supplies, often with the help of marketers. These customers often have interval meters, are in a better position than NGDCs to predict their usage, make nominations and are unlikely to look to supplier-of-last-resort service (or may not have the right to such service) in the event of a supplier failure.

By contrast, while there were certain aggregated pools of smaller core market customers receiving transportation service prior to the Choice Act, the Choice Act established the framework for the extension of choice to all of these smaller customers in the Commonwealth. These customers have different characteristics than larger customers. They are generally not in a position to predict their usage and submit nominations, they almost always are not served by interval meters, do have a right to return to supplier-of-last-resort service and, given their small individual small volumes and associated

margins, can only be practically served through aggregated pools with natural gas suppliers contracting for services such as billing with the NGDC and working with NGDCs to resolve billing and other complaints. NGDCs, to avoid potential stranded costs resulting from their supplier-of-last –resort obligations, also have statutory rights to direct assign pipeline capacity to choice suppliers and have special statutory rate obligations when customers return from a NGS default, the costs of which cannot be recovered from other PGC customers.

Given the mature long-standing larger customer transportation market serving virtually all larger volume customers in Pennsylvania, NGDCs argued the SEARCH process should be focused on the choice customer market. However, this position was not adopted by the Commission. Having made that decision, the Commission should be aware as it develops its strawman proposals, however, that NGDCs have differing statutory and regulatory obligations, and hence differing enrollment, nomination, balancing and communications rules, as well as differing information systems, to serve these very different markets. The Commission's strawman proposals should accordingly recognize these differences.

III. Supplier Coordination Tariffs

The proposed rulemaking order also indicates that the Commission intends to circulate a strawman supplier coordination tariff for review by a stakeholder process, and defines this term as follows:

SCT - Supplier coordination tariff - The formal rules and regulations of a NGDC for providing NGS service to customers. It contains a compilation of all of

the effective rate schedules of a particular company and the general terms and conditions of service.

As noted above, NGDC interactions with NGSs supplying aggregated pools of small choice customers are drastically different then NGDC interactions with larger transportation customers served by NGSs because of the dramatically different characteristics of these customer groups and the different statutory and regulatory obligations NGDCs have towards these two groups. All NGDCs, both before and after the Choice Act, had and have transportation tariffs specifying transportation rates and terms and conditions of service. These transportation tariffs also reflect rate design issues resolved in base rate proceedings. With the adoption of the Choice Act, however, a framework was established for the provision of transportation service to pools of smaller core market customers. The rules required closer communication and interaction between NGDCs and Choice suppliers than previously or currently occurs between NGDCs and NGSs acting as suppliers to larger transportation service customers. Examples of such communications include special customer enrollment rules, differing nomination and balancing responsibilities, and billing and dispute resolution rules. Accordingly, NGDCs were required as part of their restructuring filings to adopt special supplier coordination tariffs setting forth the special rules applicable to choice suppliers.

The proposed Supplier Coordination Tariff definition quoted above, however, does not reflect this common understanding of the term, and is so expansive that it would presumably encompass all or almost all of existing NGDC tariffs. If the Commission's intent is to try to standardize, to the extent possible, both tariff provisions applicable to larger transportation customers and the very different rules applicable to smaller choice

customers, then the UGI Distribution Companies would suggest the following modification to the proposed definition:

> ***SCT - Supplier coordination tariff*** - The tariff rules and regulations of a NGDC governing the provision of transportation service to end use customers or interaction with NGSs serving such customers, and tariff rules and regulations governing suppliers serving pools of core market firm service customers.

Particularly in this area of planned activity, however, the Commission should carefully consider whether there is a need to develop uniform tariff language for transportation services to larger transportation customers given that virtually all large customers are already receive transportation service, and have done so for decades without significant problems.

Moreover, it was the impression of the UGI Distribution Companies during the SEARCH process and in its own best practices collaborative that what NGSs really want are substantive changes to balancing and other rules. Such changes have costs associated with them that would require changes in NGDC rate designs. Such changes cannot be easily implemented outside of a general base rate proceeding without shifting costs between customer classes.

IV. Mandatory Business Standards

The proposed rulemaking order recognizes the distinction between adopting common business standards and changes that would require substantive program changes to migrate to a common preferred transportation and choice program designs:

> streamlining and/or standardizing certain business interactions between NGDCs and NGSs rather than requiring NGDCs to migrate to a preferred asset management system.

> Requiring all NGDCs to migrate to a preferred model for managing system assets would require comprehensive legislative changes and subsequent Commission proceedings to ensure due process related to property rights.

Order at p. 5.

However, proposed §62.185(c)(3) appears to establish mandatory standards for imbalance trading, tolerance bands, cash out and penalties and capacity that would appear to require substantive changes to existing transportation rules not in conformance with the standards. These could require additional gas supply assets to accommodate larger tolerance bands, and there would almost certainly be objections from public parties to attempts to pass the costs of such incremental assets onto PGC customers. It is not clear that the cost of such incremental gas supply assets could be recovered through the surcharge mechanism contemplated by the proposed regulations. If they are, it could result in cross-subsidization between PGC and transportation service customers.

The Commission should also recognize and clarify that the proposed standards are only intended to apply to non-choice larger customer transportation service since they would be difficult to apply to choice loads.

For example, UGI transportation service rules specify permitted balancing tolerances for larger transportation service customers. These customers must submit their own nominations since UGI is not in a position to judge their likely loads, which can vary considerably because of events such as plant shut downs or changes in process loads. The costs of the assets used to provide this tolerance are recovered from transportation customers through program and rate designs approved in base rate cases consistent with the presumptions set forth in the Commission's regulations at 52 Pa.Code §60.4(a) and (b).

In the case of choice customers, however, NGSs cannot be reasonably expected to be able to accurately judge the demands of pools of core market customers not served with interval meters. , It is also important for UGI, as system operator, to know that estimates of their consumption are being perform accurately so that it can appropriately assure system reliability while maintaining a minimal amount of assets for choice balancing purposes. Hence, UGI estimates the usage of choice customer pools served by choice suppliers, provides that number to the choice supplier, and only requires the supplier to nominate and deliver the specified amount each day, with subsequent true-ups to account for unanticipated changes in weather conditions. The costs of the assets held to provide this minimal balancing service are paid by NGSs through aggregation service tariff rates.

Given this aggregation service design, consistent with the nature of service to pools of core market customers without interval meters for which UGI has certain statutory supplier-of-last-resort obligations, and the nature of UGI's reliability obligations as a system operator, the proposed "tolerance band" standards would make no sense.

The meaning of the capacity standard set forth in §62.185(c)(3)(v) is also unclear. NGDCs hold gas supply assets used to provide supplier-of-last-resort service to PGC customers, and may hold additional assets to provide certain balancing or other services to transportation customers and NGSs serving choice customer pools. The costs of these assets, including secondary market revenues derived when they are not used for PGC or transportation services are allocated and recovered in base rate or PGC proceedings. It is not clear from the wording of this section what the Commission's intent is, but if it is to permit marketers to utilize gas supply assets used for balancing service

when they are not being utilized for this purpose, thereby transferring secondary market revenue opportunities from NGDCs and PGC customers to NGSs, then it should clearly say so and address the revenue implications of such a decision.

Overall, to address the issues stated above, the UGI Distribution Companies believe the proposed mandatory standards should only be implemented in the context of base rate proceedings, and that the Commission should clarify that the standards proposed are only applicable to non-choice transportation service. To the extent the Commission concludes that mandatory standards for choice programs are also desirable, it should establish separate standards for these programs that reflect the different nature of the services and obligations applicable to such programs, and provide for the implementation of such standards in the context of base rate proceedings.

V. Communication Standards

The UGI Distribution Companies applaud the Commission for planning to establish a working group to further address communication standards and note that the Commission has reserved the power to "direct a NGDC to install and upgrade a billing system, electronic bulletin board, software and other communication or data transmission equipment and facilities to implement established electronic data communications standards and formats."

In exercising this reserved power, however, the Commission should be mindful of the tremendous direct and indirect costs that can result from requiring changes in customer information systems. These costs must be weighed against the costs of anticipated gains that may result from the changed information systems.

VI. CONCLUSION

UGI looks forward to participating in the working groups contemplated by the Commission's Proposed Rulemaking Order. As the working groups and the Commission's regulations move forward UGI urges the Commission to be mindful of the costs of the changes it seeks and to weight these costs against the benefits to retail choice that can reasonably be expected through increased standardization.

Respectfully submitted,

Mark C. Morrow

Counsel for the UGI Distribution Companies